



Verizon Enterprise Solutions response to Ofcom's Business Connectivity Market Review Further Consultation

Verizon Enterprise Solutions ("Verizon") welcomes the opportunity to respond to Ofcom's Business Connectivity Market Review Further Consultation ("BCMR").

Verizon is the global IT solutions partner to business and government. As part of Verizon Communications – a company with nearly \$108 billion in annual revenue – Verizon serves 98 per cent of the Fortune 500. Verizon caters to large and medium business and government agencies and is connecting systems, machines, ideas and people around the world for altogether better outcomes.

Summary

Verizon accepts that the Business Connectivity Market is a complex and intricate market. Accordingly we recognise that Ofcom may wish to reconsider some of its initial proposals in light of stakeholder comments. Indeed this is important given the significance of some of Ofcom's proposals and the potentially detrimental effect they will have on stakeholders, especially BT's wholesale competitors ("OCPs").

However, we are somewhat perplexed as to precisely why Ofcom has selected the four specific issues it has identified in this consultation to review, namely:

- The geographic market in the London area – where Ofcom are now proposing that the definition of the WECLA should also include some postcode sectors in Slough.
- Service-level guarantees – Ofcom are proposing changes to the direction to correct a drafting error. The revised version will apply limits to the compensation payments payable by BT.
- Accounting obligations – Ofcom are now proposing, first, that BT should be subject to cost accounting obligations in each of the product markets in which Ofcom has proposed that it has SMP, and secondly, that BT and KCOM should be subject to accounting separation obligations in each of the wholesale product markets in which Ofcom has proposed that they have SMP.
- Circuit routing rules – Ofcom are now proposing changes to the rules that would apply to Openreach's provision of Ethernet services operating at or below 1Gbit/s.

Having reviewed the responses to the initial consultation, it is clear that there are many legitimate and significant concerns raised by stakeholders in response to Ofcom's proposals. Many are arguably much more fundamental than those identified by Ofcom, and are clearly worthy of further consultation, or at least a full re-consideration. Two examples that stand out from consultation responses are (i) Ofcom's view that a cost orientation remedy is no longer appropriate; and (ii) the approach and analysis employed in determining levels of competition in the proposed geographic markets.



Verizon therefore requests that Ofcom explains precisely why and on what basis it decided to focus on the above four issues and deemed them worthy of further consultation, whilst deciding not to re-consult on the more fundamental issues raised by stakeholders. To be clear, Verizon does not dispute that the issues under consideration in this consultation may be worthy of further consideration. However, we do not consider that they should be the immediate priority, which is the impression Ofcom is creating. It is clear from the responses to the original BCMR consultation (the “June consultation”) that there are more pressing issues that Ofcom should be responding to prior to issuing its final Statement.

Indeed, given the number of respondents who questioned the removal of the cost orientation remedy, which was almost universally opposed by OCPs, it is very concerning that Ofcom does not see the need to reconsider, or at least review, its decision in this area. We strongly hope that Ofcom is looking again at its proposals in this area, even if it does not feel there is a need for further consultation.

Since Ofcom has failed to consider any of the fundamental issues raised by industry and have instead concentrated on rectifying omissions from the original consultation, the impression is given that this reconsultation is little more than a tidying up exercise to rectify Ofcom’s mistakes. We have no issue with Ofcom correcting errors, and we hope that Ofcom will take steps to ensure they are not repeated in future, but rather our concern is that by concentrating on remedial action to the exclusion of proper consideration of the issues raised in response to the June consultation, Ofcom is in fact making a further error.

The remainder of this response focuses on the four issues Ofcom has identified for revision as well as commenting on Ofcom’s further consideration of its MISBO market power assessment. We also set out some final comments on the issue of cost orientation.

Geographic market in the London area

If Ofcom’s analysis, as presented in the June consultation, as to the competitive conditions that exist in the WECLA region had been compelling, then Verizon would be less inclined to oppose this proposal. However, as explained in our response to the June consultation, we have grave concerns over the way Ofcom reached its conclusions on the WECLA. In short we consider that the decision to extend the Central and East London Area (“CELA”) to incorporate the area covered by the WECLA was reached on a flawed analysis of the competitive conditions that exist in the WECLA. As stated in our previous response, we consider that Ofcom should have undertaken a disaggregated analysis of the part of the WECLA which is not in the CELA, before considering whether competitive conditions across the WECLA as a whole are homogenous.

We note that Ofcom has not responded to this criticism and has not disclosed the disaggregated data in order to justify its initial findings. We are disappointed that Ofcom has chosen not to address this point in its further consultation, when this would appear to be a natural opportunity to do so. Without such disclosure, we are



unable to accept that the proposed de-regulation is based on solid evidence and is a true and fair representation of the competitive landscape. Accordingly, we consider that this proposed further extension of the WECLA is based on the same flawed analysis and simply perpetuates the same error.

The complete U-turn by Ofcom in respect of the Slough postcode sectors lends further weight to this view. Ofcom states that it was aware of the high network reach of these postcodes prior to the June consultation, but decided not to extent the CELA to Slough due to the lack of continuity as a result of the SL3 0 exclusion. Although this raised concern from **only one** CP, Ofcom has revised its approach stating that it is following a 'sensible approach when defining geographic markets'. This begs the question of what approach Ofcom was taking previously, if in fact it was not a 'sensible' approach?

In light of these points, Verizon does not agree with Ofcom's proposal to include the Slough sectors in WECLA and maintains its view that there is not a similar, comparable, high density of business customers and network build by market players for the extended WECLA mapped out by Ofcom as there is in the CELA.

Furthermore, Verizon is concerned that Ofcom has deemed it appropriate to revisit its findings on the extent of the WECLA seemingly on the basis of submissions from BT alone. At the same time it has ignored legitimate concerns raised by a significant number of OCPs as to the process Ofcom adopted in determining the existence of separate geographic markets. Whilst Ofcom will undoubtedly respond to these concerns in its final statement, given the nature of this proposed revision surely Ofcom should have responded now, in this consultation? This would have provided Ofcom with the opportunity to legitimise its position and justify its stance in considering an extension to a proposed designated geographic market. The fact that it has not done so serves only to strengthen our concern about the legitimacy of the original analysis and conclusions drawn.

Service-level guarantees

Ofcom states that its revision of the SLG proposals corrects an inadvertent omission from the June consultation and just reapplies the compensation caps that were imposed as a result of the previous, 2007/08, market review. Verizon does not dispute this; however we do consider that Ofcom should take the opportunity to consider whether the SLGs remain fit for purpose and whether they incentivise BT appropriately.

Accounting obligations

Ofcom, in this consultation, is proposing to impose cost accounting obligations on BT in each of the markets where there has been a finding of SMP. Verizon considers that, irrespective of the merits or otherwise of this proposed additional obligation, Ofcom's proposed remedies taken as a package are highly flawed and will not achieve their overall objective. This is because without the imposition of a cost orientation obligation they will not act as a credible deterrent against BT's propensity



to set excessive charges for services in this market. We address these concerns at greater length later in this response.

Verizon fails to see how Ofcom's current proposals in terms of charge control sub caps and an obligation to deliver DLRIC and DSAC figures to Ofcom alone (i.e. no visibility to CPs in real time) will be sufficient to constrain BT's charges, given that a charge control, reinforced by a cost orientation obligation failed to do so during the period of the last charge control. Ofcom showed itself to be unable and/or unwilling to monitor and effectively scrutinise such data in the past. Under its current cost accounting proposal OCPs would become totally reliant on Ofcom's vigilance in the future, and this does not provide anywhere near the level of certainty or reassurance that the industry needs. The fact that cost allocation rules are being relaxed, despite findings of excessive charging by BT in the recent past in more than one market, is not only mystifying but borders on an abdication by Ofcom of its duties.

The proposal that DSAC and DLRIC information be provided to Ofcom alone is, with respect, absurd. Ofcom has shown over the last [8] years that it has no desire to monitor compliance with those thresholds of its own accord. On the contrary, Ofcom has relied on disputes submitted by CPs. Unless Ofcom plans to change that approach and pro-actively scrutinise BT's information, Ofcom's suggestion in the reconsultation does not make any sense. In addition, it is in direct contravention of the requirements of the Communications Act and the Framework Directive that regulation be transparent.

Circuit routing rules

Overall, Verizon is supportive of Ofcom's proposed changes to the circuit routing rules, as they represent a less restrictive and more simplified arrangement. It is also important that BT has an obligation to continue to provide wholesale disaggregated access and backhaul Ethernet services and does not have the ability to block reasonable requests for network access.

As for the changes to the list of BT operational buildings assigned to each TAN, Verizon does not believe this will have any impact on us, so does not offer any further comment on Ofcom's proposals.

SMP assessment of the MISBO market

Verizon has very significant concerns about Ofcom's decision to reconsult on this issue. The reconsultation seems to have been based on information submitted by BT; but not verified by means of s.135 notices nor checked against other comparable data.

On the face of it, the BT arguments are deeply implausible. For example, it **may** be true (although it has certainly not been tested) that large businesses with data requirements above 1Gbit/s cluster in areas with multiple networks. However, on its own this means nothing in terms of market definition and market power. The



consultation begs an extraordinary number of questions: what is to happen to businesses that cannot relocate in the way that BT has suggested? If there is truth in BT's suggestion, why can it not be dealt with in the same way as the WECLA?

In short, Verizon is astonished that Ofcom believes that this sort of approach to determining SMP is appropriate and hopes that Ofcom will not continue to consult in a way which only looks at the issues raised by BT at the expense of the other serious issues raised by CPs.

As to the question of availability of dark fibre, Verizon would contest the suggestion that dark fibre is readily available. In our experience, neither BT nor other large network operators are willing to supply dark fibre, so to base any finding or lack of finding of SMP on dark fibre availability would be a divergence from evidence based regulation.

Accordingly, Verizon does not consider the evidence available supports a view that competitive conditions exist for the MISBO market on a national basis outside of CELA. An assessment of Verizon's on-net and near-net capabilities for GigE circuits provides an indication of our potential access to this market compared with BT's and clearly demonstrates the degree for potential competition is extremely limited.

Furthermore, Verizon considers that, whilst a few other carriers have slightly greater access than Verizon, an assessment of carriers network build by post code indicates that more than 58% of the country does not exhibit the potential for truly competitive conditions in the MISBO market (see Fig 1 below). Even where our analysis shows that another carrier is in the same post code area as BT, unless they are in the same building their dig costs are likely to mean that they will be uncompetitive.

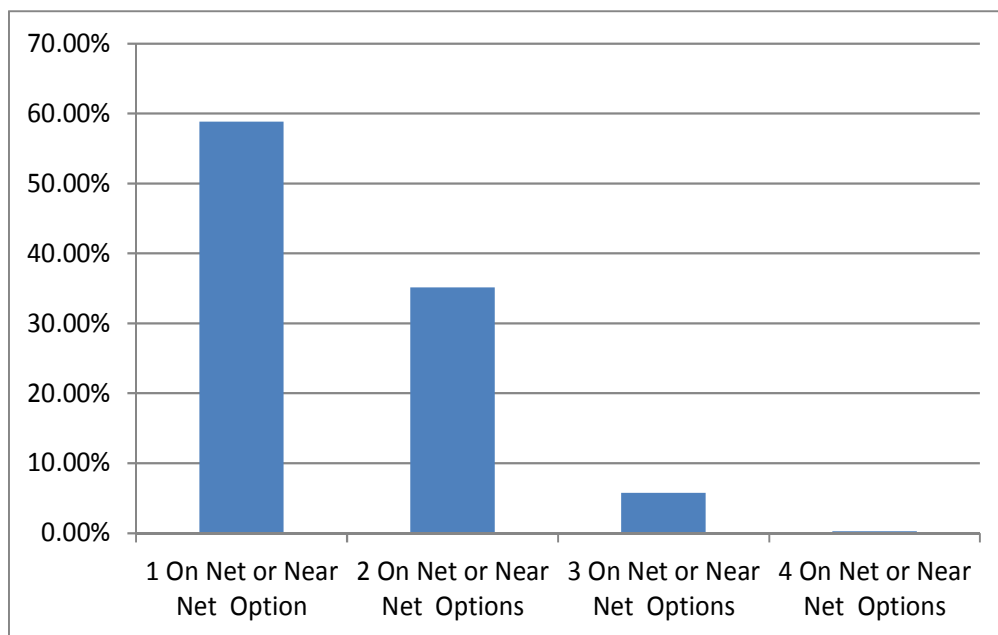


Fig1. Carrier on-net and near-net capabilities by post code (excluding WECLA)



In summary, Verizon does not consider that the supply of MISBO services can be considered as being competitive throughout the UK and is anticipating that Ofcom will reach the same conclusion once it has considered all the evidence.

Cost orientation

We now turn to an addition issue which we consider Ofcom should also review following the responses from stakeholders to the initial BCMR consultation.

As indicated earlier in our response, it seems strange that Ofcom has not taken the opportunity of this further consultation to reassess its position on the proposed removal of the cost orientation remedy from the markets in question. It is worth recapping Ofcom's recent work in this area, at least from an external perspective.

Ofcom issued a call for inputs on cost orientation (among other things) over a year ago.¹ Following stakeholder responses, Ofcom remained silent on its thinking or progress on this subject for approximately six months.

Then in June this year, Ofcom issued the June consultation. The June consultation heralded a complete revision in Ofcom policy regarding cost orientation – and a corresponding shift in its thinking on the effectiveness of charge controls – at least in relation to the business connectivity markets.

Ofcom now appears to consider that relatively minor adjustments to existing charge controls will sufficiently mitigate the risk of excessive pricing by BT (although what it means by excessive pricing is not made clear). This is despite BT's history of sustained excessive pricing over several years in both the PPC and Ethernet markets. As a result, Ofcom feels that the cost orientation remedy can simply be removed.

Ofcom offered a derisory level of explanation for its policy change. It is beyond belief that Ofcom considers the justification that it set out was even close to adequate. Ofcom's arguments in support of such a radical change were, in the main, set out in a *single paragraph* of the LLCC – namely paragraph 5.72.

Ofcom received a very strong response to this proposal. OCP after OCP has lined up to protest against this relaxation of regulation on BT. Economic experts provided independent analysis on the detriment to competition and consumers that could be expected as a result.

Despite this, Ofcom has chosen to remain silent on this issue in the further consultation, save for a brief comment announcing its intention to issue more thinking on cost orientation at some later point in the year². It is unclear what form this

¹ Review of cost orientation and regulatory financial reporting in telecoms - Call for inputs
8 November 2011

² Business Connectivity Market review – Further consultation Sec 4.24



thinking will take, but even if it is a consultation (which looks increasingly doubtful) it will come far too late to be taken account of in the BCMR final Statement.

Given Ofcom's policy U-turn on cost orientation in the business connectivity markets, and the inevitable level of concern expressed by industry in relation to this, Ofcom's announcement of a publication is perplexing.

Not least, Ofcom's timing for considering the cost orientation issue is clearly out of sync with the relevant, impacted market reviews. This inevitably raises the question of whether Ofcom commenced its review of the Business Connectivity Market with pre-conceived aims and objectives. It also suggests that Ofcom was developing policy on cost orientation which it failed to disclose in the June consultation (or indeed in this further consultation).

Even the choice of words to describe the future cost orientation document reinforces the view that this is a closed issue as far as Ofcom is concerned and there is no intention to actually consult on the issue.

It would be interesting to know whether Ofcom considers that it has acted in a transparent and appropriate manner in relation to communicating and consulting on cost orientation over the last year or so. It must surely recognise the value placed on this remedy by OCPs in deterring excessive pricing by BT and providing a channel to compensation in the event that BT failed to comply with the remedy. It must equally have recognised that its proposal to remove the remedy would need adequate justification backed up by compelling evidence – and at the time of the original proposal in June, not months later.

Instead it has issued a call for inputs on the subject, followed by a period of silence for six months, followed by a consultation to remove it with virtually no explanation, followed by the promise of a "publication". Ofcom should understand that from an external perspective this is viewed in a very negative light.

This is a critical issue for OCPs, and it will have a very material bearing on the perception of fairness and accountability in the relevant markets. Ofcom must realise that it will seriously undermine confidence and trust in the regulatory regime if it does not address industry concerns adequately. Given its intention to issue a publication at some future time on cost orientation, we are very concerned that this is an attempt to deflect criticism from its proposed final conclusions in the BCMR. We urge Ofcom to concentrate its resources on re-considering cost orientation as a valid remedy in the BCMR markets, rather than issuing some as yet undefined publication on the matter at some time in the future.

Verizon Enterprise Solutions
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